

Section III Asset Management

Chapter 2 Controlling Documents

2.1

Introduction

The Section 232 mortgage insurance documents are the controlling documents which detail program requirements and obligations. These documents are comprised of contracts (Agreements), certifications, forms, and regulations. The documents discussed in this Chapter were published pursuant to the Paperwork Reduction Act (PRA) and are available on the Section 232 Program website.

2.2

Regulatory Agreements

Regulatory Agreement. The regulatory agreement is the contractual document under which the Borrower, Operator and, if applicable, the Master Tenant are regulated by HUD, as long as HUD is the insurer or holder of the mortgage. Therefore, depending on the Borrower and Operator structure, the project may have one or more of the following regulatory agreements:

1. Healthcare Regulatory Agreement – Borrower, or Borrower Regulatory Agreement (Form HUD-92466-ORCF),
2. Healthcare Regulatory Agreement – Operator, or Operator Regulatory Agreement (Form HUD-92466A-ORCF), or
3. Healthcare Regulatory Agreement – Master Tenant, or Master Tenant Regulatory Agreement (Form HUD-92337-ORCF).

Depending on the date an FHA-mortgage was insured, the insured mortgage may have earlier versions of these documents, which do still apply in full force and effect, and this Section III of this Handbook does apply to those insured mortgages.

If the Borrower and Operator are the identical legal entity, then that entity shall sign both the Borrower Regulatory Agreement and the Operator Regulatory Agreement. The regulatory agreement is recorded in the land records and thus is an encumbrance on the property. HUD will agree to release the regulatory agreement when the FHA-insured loan is paid in full, either at maturity or upon prepayment. (The prepayment approval process is in Asset Management,

Chapter 3.3.2.) The Borrower or Operator shall provide its Account Executive (AE) with a written request with a legible copy of the recorded regulatory agreement attached. The AE will forward both documents to Headquarters, Office of General Counsel, Insured Housing Multifamily Mortgage Division for processing.

2.3

Mortgage and Mortgage Note

- A. **Mortgage:** A mortgage is a written instrument which evidences an interest in land or real property and provides security for the performance of a duty or the payment of a debt. The FHA mortgage is one in which the loan has been insured by the Federal Housing Administration (FHA).
- B. **Mortgage Note:** A mortgage note is executed for all insured mortgages. It is the written document that evidences a loan for which real estate has been offered as security and includes an unconditional promise by the Borrower to repay the debt on a specified date. It is also the document that FHA endorses as evidence of its insurance commitment. It sets forth the original amount of indebtedness to the Lender, the interest rate, and the manner in which the debt will be repaid.

2.4

Uniform Commercial Code (UCC) Filing

Uniform Commercial Code. The Uniform Commercial Code (“UCC,” or “the Code”), deals primarily with transactions involving personal property (movable property), but not real property (immovable property). Article 9 governs how security interests may be obtained in personal property that a Borrower and a Lender agree will serve as security for payment of specified debts. Fundamental concepts under Article 9 include: how a security interest is imposed on property (“attachment”); how security interests are made complete (“perfected”); and what remedies are available to the secured party if the debtor defaults in payment or performance of the secured debt or obligation.

2.5

Operating Lease

Operating Lease. The Operating Lease (or Agreement) provides the Operator with the use of the property for a particular period of time and sets forth the Borrower’s and Operator’s responsibilities and obligations. The terms of the Operating Lease must be consistent with Section 232 of the National Housing Act, Section 232 Regulations and Program Obligations (see Production, Chapter 8).

2.6

Master Leases

Master Lease. Master Leases, also known as Sandwich Leases or Credit Pass Throughs, are used by national and regional healthcare Borrowers. These transactions create a tiered structure with a Master Tenant leasing multiple projects from the Borrowers, and then entering into subleases, which are sometimes referred to as master subleases, with the entities that will operate the healthcare facilities. Through the master lease agreement, the Master Tenant agrees, among other things, to pay the Borrowers' rent necessary to satisfy the Borrower's financial obligations under the FHA-insured mortgage. Also, the sublessees (or subtenants) are required, among other things, to agree to contribute additional amounts when needed and as available to cover any shortfall in the rent that the Master Tenant owes to the Borrower (see Production, Chapter 13).

2.7

Accounts Receivable Financing, Deposit Account Control Agreements (DACAs), Operator Bank Accounts and Deposit Account Instruction Service Agreements (DAISAs)

- A. **Accounts Receivable (AR) Financing.** A majority of skilled nursing facility operators now use accounts receivable (AR) loan financing mechanisms to ensure that adequate cash flow is available to meet ongoing operating expense needs. Typically, the Operator provides patient services which are reimbursed by Medicaid and Medicare 30 to 90 days after the services are provided. The timing of these reimbursements varies from state to state and can be subject to significant delays. The remaining patients either pay for their services from their own private resources (private-pay) or have private insurance coverage. Absent AR lines of credit, Operators may be at risk of experiencing short-term cash liquidity shortfalls. The AR line of credit provides a source of funds to sustain ongoing operations until Medicaid and/or Medicare reimbursement funds are received. In addition, the AR Lender supplements ORCF's oversight as a third party monitoring the financial operations of the Operator. This results in additional oversight and proactive intervention with the Operator if unusual or troubling financial trends appear (see Production, Chapter 15, and Asset Management, Chapter 10).
- B. **Deposit Account Control Agreement (DACA).** The accounts receivables ("AR") of the Operator of a project subject to a FHA-insured loan, constitutes "project income." There are two types of project income: non-governmental and governmental receivables. The Deposit Account Control Agreement ("DACA") addresses the non-governmental receivables. A security interest in those AR must be executed by the Operator, via a security agreement. Pursuant to UCC §9-104, a DACA is used to perfect ORCF's and the Lender's security interest in the Operator's deposit accounts. A DACA is an agreement made among a secured party (generally, the FHA Lender), a debtor (generally, the Operator, whether the Borrower or lessee), and depository bank (the bank at which the Operator maintains its deposit

accounts) in which the debtor has agreed that the bank will comply with the secured party's instructions regarding disposition of the funds in the debtor's deposit account without further consent by the debtor. DACAs are referred to by various names, including Blocked Account Agreements, Lockbox Agreements and Springing Lockbox Agreements (see Production, Chapter 15 and Chapter 16, and Asset Management, Chapter 10).

- C. **Operator Bank Accounts:** It is understood that the Operator will typically maintain at least two separate bank accounts. The first account, the Governmental Healthcare Receivables Account (GHR Account), is an account into which all Medicare/Medicaid receivables are deposited. It is expected that the FHA Lender, depository bank and, where applicable, the AR Lender will enter into a Deposit Account Instructions Service Agreement ("DAISA") that requires the depository bank to "sweep" the GHR Account daily (or less frequently with HUD approval) such that all funds deposited in the GHR Account are transferred to a second account of the Operator, known as the "Operating Account" (see Production, Chapter 16).
- D. **Deposit Account Instructions Service Agreement (DAISA) guidelines:** A DAISA refers to the instructions provided to the bank by the debtor that details how the bank is to dispose of governmental healthcare funds in the GHR Account. The DAISA must not grant the FHA Lender the right to direct disbursements from the GHR Account as in a DACA in order to avoid a conflict with applicable healthcare program restrictions (e. g. the Medicare/Medicaid anti-assignment provisions). Unlike a DACA, a DAISA should be terminable by the Operator in order to comply with all applicable healthcare program restrictions (e. g. Medicare/Medicaid anti-assignment provisions). The Security Agreements shall also provide that the Operator must procure the FHA Lender's written consent prior to closing a deposit account subject to a DAISA or terminating the DAISA FHA Lender (see Production, Chapter 15 and Chapter 16, and Asset Management, Chapter 10).

2.8

Management Certification

The definition of a Management Agent, including the distinction between a Management Agent and an Operator, is discussed in Production, Chapter 8 and Asset Management, Chapter 8. A party who is deemed a Management Agent by HUD, rather than an Operator, must execute a Consolidated Certification – Management Agent (Form HUD-90017-ORCF).